



**STATEMENT OF
DAVY G. LEGHORN, ASSISTANT DIRECTOR
NATIONAL VETERANS EMPLOYMENT AND EDUCATION DIVISION
THE AMERICAN LEGION**

BEFORE THE

**SUBCOMMITTEE ON ECONOMIC GROWTH, TAX, AND CAPITAL ACCESS
COMMITTEE ON SMALL BUSINESS
UNITED STATES HOUSE OF REPRESENTATIVES**

ON

**“EXPLORING CHALLENGES AND OPPORTUNITIES FACED BY UNDERSERVED
BUSINESSES IN THE 21ST CENTURY”**

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Chairman Kim, Ranking Member Hern, and distinguished members of the Subcommittee on Economic Growth, Tax, and Capital Access, on behalf of National Commander Brett P. Reistad and the nearly two million members of The American Legion, we thank you for the opportunity to testify before you today on exploring challenges and opportunities faced by underserved businesses in the 21st century. We commend your leadership in exploring the challenges faced by underserved businesses – particularly veteran-owned small businesses (VOSB’s). The American Legion looks forward to working with this committee to continue fostering policy and initiatives that empower veterans to pursue the American entrepreneurial spirit.

BACKGROUND

Veterans continue to serve their country long after their military service by employing 5.03 million Americans, managing receipts in excess of \$1.14 trillion dollars, and accounting for nearly 10% of U.S. Small Businesses¹. Despite strong numbers, veteran-owned small businesses continue to experience unnecessary bureaucratic obstacles and difficulties in securing government contracts, as was evident in the landmark *Kingdomware Technologies, Inc. v. United States (U.S.)* court case.

In response to the need of the VOSB population, The American Legion established a taskforce of volunteer small business owning legionnaires in 2011. The American Legion Small Business Taskforce works to identify critical issues impacting VOSB’s, along with working to ensure that viable and workable solutions are examined. The goal and mission of the Small Business Task force is to furnish The American Legion with first-hand experience and insight into the VOSB community, so we can accurately advocate for them before this critical committee and Congress as a whole.

The American Legion responded to concerns from our Small Business Task Force, by establishing small business counseling services for VOSB’s or veterans hoping to start a business. We rely on our taskforce volunteers to take on advisory roles in our entrepreneurship services and to lend their

¹ Small Business Administration: Office of Advocacy. Veteran-Owned Businesses and Their Owners: Data from the U.S. Census Bureau’s Survey of Business Owners (2017). Washington, D.C.

expertise in small business advocacy. The Small Business Taskforce is the national voice of the veteran entrepreneur.

We assist veterans in establishing their disability claims, enabling the veteran to then obtain their Service-Disabled Veteran-Owned Small Business (SDVOSB) or Veteran-Owned Small Business status under the Veterans First Contracting Program (also known as Veterans First). Through our initiative, our efforts led us to participate in the Verification Assistance Counseling Program through Veterans First since its inception. The American Legion, through our Small Business Task Force, assists veteran small business owners in obtaining verification or maintain verification status when facing debarment. It is important to note, that our services are not exclusively offered to the two million members of The American Legion, but to all veterans who express a need or interest.

The American Legion's efforts to advocate on behalf of our nation's veteran small business owners does not stop at the chamber doors of Congress, but it also extend to the chambers of the justices, federal agencies, and the White House. The American Legion supports veteran-owned businesses as they continue to endure legal efforts to circumvent and subvert PL 109-461's Veterans First Program. The American Legion submitted an amicus brief in support of Kingdomware Technologies with the federal appellate court and Supreme Court. We also signed on to an amicus brief in support of veteran-owned businesses in *PDS Consultants, Inc. v. U.S.* The American Legion continues to relentlessly support this committee and this Congress in eliminating artificial roadblocks that are detrimental to our veteran entrepreneurs. Our efforts will continue until VA procurements meet the letter and intent of the Veterans First Program.

The court decision in *Kingdomware Technologies, Inc. v. U.S.* was a significant victory for veteran small business owners, yet significant challenges remain. The American Legion believes these set-asides should expand beyond the Department of Veterans' Affairs (VA) and across the federal government. Further, The American Legion commends the Small Business Administration's (SBA) work through the Office of Veterans' Business Development (OVBD), but strides remain to be made. With only 22 Veterans Business Outreach Centers (VBOCs) across the country, rural Americans and those living in Puerto Rico, Guam, the Virgin Islands, and American Samoa often lack access to resources. Without access to resources, veterans who participate in the Boots to Business Program (B2B) as part of the military's Transition Assistance Program (TAP) have no method of follow-up. Often we see veteran small businesses owners come out of B2B – singularly focused on creating a business plan, without an understanding of how to establish business governance or conduct the requisite administrative tasks to be recognized as a business in their state or territory. Lastly, The American Legion supports initiatives and organizations that advance emerging internet-based and peer-financed alternative capital options that focus on funding veteran-owned small businesses.

REALIGNMENT OF FINAL RULES AND INTENT AFTER KINGDOMWARE

The greatest detriment to the veteran small business industrial base has been misinterpretation of legislation stipulating SDVOSBs as a preferred contracting group for the federal government. The American Legion expects the outcome of *Kingdomware Technologies, Inc. v. U.S.*² will reinterpret the rules of Veterans Entrepreneurship and Small Business Development Act of 1999.

² *Kingdomware Technologies, Inc. v. United States*, 579 U.S. (2016)

The Justices of the Supreme Court were clear in their unanimous opinion; the intent of the three percent set-aside goal for SDVOSBs in the Veterans Entrepreneurship and Small Business Development Act of 1999 is to “encourage small business” and not for the sole purpose of fulfilling a quota.³ The Supreme Court opined that the subsequent enactment of the Veterans Benefits, Health Care, and Information Technology Act of 2006 was ancillary in nature to the Veterans Entrepreneurship and Small Business Development Act of 1999 and shares ilk intent.

The nexus in the intent of the two separate and distinct programs has broader implications for the federal government. The opinion of the court advises agencies that the reasoning behind the set-aside goals applies to government-wide SDVOSB programs and agency-specific programs (i.e. Veterans First Contracting Program at the Department of Veterans Affairs).

Initially, the Small Business Development Act of 1999 and Veterans Benefits Act of 2003 gave SBA and other federal agencies authority to increase VOSBs industrial base. In 2005, SBA and the Federal Acquisition Regulatory (FAR) Council issued concurring final rule comments stating SDVOSB Programs were not developmental in nature⁴. SBA and the FAR Council concurred SDVOSB programs are localized to the benefits in federal contracting and the sole purpose is to increase participation of established SDVOSBs already within the federal marketplace. SBA and the FAR Council were clear that the SDVOSB Program was not meant for business development or growing an industrial base. The reversal in rule-making is arguably contrary to the intent of Congress and was widely unpopular.

As result of the SBA and FAR Council’s rule-making comments, the SDVOSB Program developed purely into a set-aside program where the only metric for success was measured by dollars out the door as opposed to the wellbeing of the veteran small business industrial base. A program geared to meet a minimum threshold of dollars-spent does not encourage growth of the industrial base. As a result of the aforementioned objective, the vast majority of the three percent federal set-aside is localized to a small group of companies. The culmination of a set-aside program without business development in mind, coupled with measuring success on dollars out the door vs. the creation of new business led to the program as it currently exists — it fails to meet the intent and the letter of the law.

Kingdomware Technologies, Inc. v. the U.S. was groundbreaking in that the decision harkened back to Congress’ original intent at creating an SDVOSB Program with business development and the growth of the industrial base as a part of the framework. The American Legion expects the decision to result in SBA and the FAR Council reconsidering their 2005 final rule comments thus realigning them with the Court’s decision and original congressional intent. Further, any subsequent rule change for the SDVOSB Program must incentivize agencies to take into account the diversity of SDVOSBs participating in the marketplace and not simply by a dollars out the door figure.

³ *Kingdomware Technologies, Inc. v. United States*, 579 U.S. (2016) (“In an effort to encourage small businesses, Congress has mandated that federal agencies restrict competition for some federal contracts.”).

⁴ *Ibid*

To SBA's credit, they have begun examining solutions towards the problems that stemmed from the 2005 rule-making decisions. OVBD created several successful entrepreneurship development programs under a separate authority to grow the veteran small business industrial base. Also, work is already underway at SBA to revise the small business goal's grading criteria to ensure that the total federal set-aside spend is spread out to more veteran-owned small businesses. The American Legion sees the Kingdomware decision as a catalyst that shall hasten many programmatic improvements that the SBA has already been working towards and finally recognize the developmental intent of the SDVOSB program. The American Legion believes the inclusion of SDVOSBs into the SBA's 7(j) programs is a good start.

VETERANS FIRST CONTRACTING PROGRAM BEYOND VA

The American Legion supports the expansion and improvement of all entrepreneurship programs, loan programs and numerical goals for all veterans to compete in government procurement and contracts.⁵ This is why we believe the *Kingdomware* decision lends credibility for the additional tier of veterans' preference to exist within existing federal contract set-aside programs. This preference can now be legislatively extended government-wide or at the very least, to several other agencies.

Mandated in 2006 by Public Law 109-461 and, before that, by President Bush's 2004 Executive Order 13360, VA was entrusted with a fiduciary responsibility to grow the veteran small business industrial base. The American Legion believes that the federal agencies that send our servicemembers to war should share in VA's responsibilities. The Department of Defense and the Department of Homeland Security should have the moral imperative to enforce the veteran's preference in their purchases. To this end, The American Legion asks that the Veterans First Contracting Program within VA should be legislatively extended to the aforementioned agencies requiring the same preference in set-aside authorities.

OVBD AND BOOTS TO BUSINESS

Since its implementation in 2012, the Boots to Business (B2B) capstone course taught as a part of the military's Transition Assistance Program (TAP) has been very successful. SBA was the first to pilot and then implement their portion of TAP in compliance with the directives of the VOW to Hire Heroes Act of 2011. B2B is a lean program, administered solely through SBA's 22 Veterans Business Outreach Centers (VBOCs). We are proud to report that during the recent government shutdown, 95 percent of the scheduled B2B sessions taught on and off military bases were administered. For the last five years, the two day B2B curriculum has been the litmus test that has helped veterans launch their businesses.

B2B is currently a non-mandatory portion of a three-tracked capstone course available to Servicemembers within two years of their date of separation. In the 2019 National Defense Authorization Act, there was an attempt to make at least one of the TAP capstone courses mandatory. The American Legion supports this attempt and hopes this will expose more servicemembers to SBA and their partners.

⁵ The American Legion Resolution Number 21, 2018.

The American Legion believes we should increase the pool of servicemembers eligibility for SBA programs. Currently, Guard and Reserve members are not eligible for vet small business development and entrepreneurship programs until after they are activated under Title 10. The American Legion recognizes that our National Guardsmen are often deployed under Title 32 and the law must be changed so that they too are eligible for SBA programs. This is why The American Legion supports legislation similar to H.R. 7199, the National Guard and Reserve Entrepreneurship Act of 2018, introduced during the 115th Congress, that proposes amending 15 USC §636 to increase the eligibility of military-focused SBA programs to those who have “[been] ordered to perform active-duty service for more than 30 consecutive days”.

Increased utilization of SBA’s military and veteran-centric programs will require more VBOCs. The American Legion supports the creation of more VBOCs to include one in every state and the territories. Puerto Rico, Guam, Virgin Islands, and American Samoa are often overlooked for veterans programs and services, despite the heavy military presence and armed services recruitment efforts that occur in these places. That is why American Legion Resolution No. 26 supports Section 301 of H.R. 225, the Puerto Rico Small Business Assistance Act of 2019. The American Legion asks this committee to consider creating VBOCs in other locations where military and veterans are heavily populated.

LENDING PROGRAMS

The 7(a) program is the SBA’s flagship program. SBA does not directly provide the funds to a small business, but rather issues a guarantee to the bank that should the small business default the SBA will back the loan. 7(a) loans utilization for veterans have seen a recent decline, from \$1,370,204,100 in 2015 to \$1,064,474,800 in 2018, but there is no reason to be alarmed considering the innovation and diversification of small business lenders within the last decade⁶.

SBA’s flagship program is the 7(a) loan. The 7(a) loan program is operated through banks, but banks have been a diminishing source of credit for small business according to the National Federation of Independent Business⁷. The downward trend has persisted throughout the last decade due to a combination of factors, but mainly because bank-based programs have rigid structures that are less effective at meeting the mercurial needs of small businesses.

According to the Federal Financial Institutions Examination Council, the number of commercial banks has been in steady decline since the 1980s. The US lost over 2000 commercial banks since 2009⁸, and new banks are not forming. The banking industry is consolidating under financial industry giants.

Large financial institutions avoid small business lending because small loans are time intensive for their amount, hard to securitize, and expensive to underwrite and service, which is why

⁶ U.S. Small Business Administration: Office of Capital Access. *Veteran Lending Update: December 6, 2018*.

⁷ Small Business, Credit Access, and a Lingering Recession. (2012, January). Retrieved February 1, 2019, from <http://www.nfib.com/Portals/0/pdf/allusers/research/studies/small-business-credit-study-nfib-2012.pdf>

⁸ Commercial Banks in the U.S. (2018, December 13). Retrieved February 1, 2019, from <https://fred.stlouisfed.org/series/USNUM>

community and regional banks form the backbone of the 7(a) and 504 loan programs. The decline in community banks has inadvertently led to the diminished utilization of 7(a) loans.

The downward trend in bank creation inadvertently spurred diversification in the financial industry. Alternative lenders began to take over the traditional roles of community banks when it came to small business lending. Coming out of recession, when banks were reticent to make riskier loans, the market still found a way to link investors to new and innovative products. The alternative lending industry gained significant traction within the last five years with online peer-to-peer and social lending products outpacing Securities Exchange Commission regulations.

According to statistics from SBA's Office of Capital Access, veteran usage of the micro-loan program is trending upwards annually from \$2,083,315 in 2013 to \$3,705,147 in 2018. The American Legion had the opportunity to work with the Latino Economic Development Corporation (LEDC) to conduct outreach to local veteran start-ups about micro-lending. It is important to note, that during the 2018-2019 government shutdown, community development financial institutions (CDFIs) were unable to process loans and provide services to veterans. To prevent this from negatively impacting veteran owned small businesses, The American Legion asks that SBA's loan processing staff be designated "essential" workers during a government shutdown.

The lending renaissance experienced in the aftermath of the recession diversified and reshaped small business financing. Traditional bank-based lending is just one of many ways to make credit accessible to small businesses. Microloans, social financing, peer-to-peer lending, private equity, venture capital, and angel investors have gained a stronger foothold, and this diversity has been a win for small business because they are no longer solely reliant on banks. For the reason that small business financing is no longer dominated by traditional lenders, SBA needs to reconsider the promotion of 7(a) loans as their flagship product. An SBA grantee's primary metric for success is the capture of 7(a) loan dollars; this ultimately bleeds over into the administration of entrepreneurial development programs including B2B, where there is a push to get small businesses ready to go to the banks to utilize SBA's premier loan product. ED programs should be helping businesses get financing. Often, the first interface a small business owner has with the SBA or a grantee is when they need financing; however, bank loans currently comprise just a limited fraction of small business borrowing.

This is the right time for SBA to re-evaluate their goals and metrics that the ED programs support. It's time to update an aging lending program and time to prioritize exposure of veteran entrepreneurs to alternative lenders. Through American Legion Resolution 152: The American Legion supports initiatives and organizations that advance emerging internet-based and peer-financed alternative capital options that focus on funding veteran-owned small businesses.

CONCLUSION

Chairman Kelly, Ranking Member Hern, and distinguished members of this critical committee, The American Legion thanks you for the opportunity to explain the position of our nearly two million members of The American Legion. Questions concerning this testimony can be directed

to Jonathan Espinoza, Legislative Associate, in The American Legion's Legislative Division at (202) 861-2700, or jespinoza@legion.org